

Annual Profit Plan and Supporting Schedules

Overview

The **Annual Profit Plan** (also called the **Master Budget**) is the company's comprehensive financial plan for the coming year. It expresses management's **operating and financial goals** and serves as a **control and coordination tool**.

The Budgeting Cycle

The **budgeting cycle** is an ongoing process that continues throughout the year.

Key Steps:

1. **Planning Phase**
 - Managers at all levels, using past data and future expectations, plan performance for the next period.
 - The result = **Annual Master Budget (Profit Plan)**.
 2. **Performance Reporting**
 - Throughout the year, **actual results** are compared with **budgeted results** (monthly/quarterly).
 3. **Variance Analysis**
 - Management accountants help investigate variances.
 - **Adjustments** are made to operations or the budget itself if external conditions change.
 4. **Continuous Monitoring**
 - Managers monitor market feedback and external conditions to prepare for the next cycle.
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Development of the Annual / Master Budget

Output:

A full set of **budgeted financial statements**, including:

- Budgeted **Balance Sheet**
- Budgeted **Income Statement**
- Budgeted **Statement of Cash Flows**

These are prepared:

- By **responsibility center**

- Then consolidated into **company-wide** budgeted statements
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Participative (Bottom-Up) Budgeting

Definition:

Involves **lower-level managers** in preparing the budget since they know practical details of operations.

Benefits:

- Higher **accuracy**
- Greater **motivation and ownership**
- Better **coordination and communication**

Note:

Even with participative budgeting, **top management** must:

- Set **goals**
 - Define **priorities**
 - Provide **support and oversight**
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Structure of the Master Budget

The Master Budget = **Operating Budget + Financial Budget**

♦ A. Operating Budget

It includes the **Budgeted Income Statement** and its supporting schedules.

Components:

1. **Sales Budget** – starting point for all budgets
2. **Production Budget** – based on sales and inventory needs
3. **Direct Materials Usage Budget**
4. **Direct Materials Purchases Budget**
5. **Direct Labor Usage Budget**
6. **Manufacturing Overhead Budget**
7. **Ending Inventories Budgets** (Finished Goods, Materials)
8. **Budgeted Cost of Goods Manufactured**
9. **Budgeted Cost of Goods Sold**

10. **Nonmanufacturing Budgets** (e.g., Selling & Administrative)

11. **Budgeted Income Statement**

- **Selling & admin assets** → increases depreciation and fixed assets.
- **Financing activities** → affect both **Cash Budget** and **Balance Sheet**.

◆ **B. Financial Budget**

Covers the company's **financial position and cash planning**.

Components:

1. **Capital Expenditures Budget**
2. **Cash Budget**
3. **Budgeted Balance Sheet**
4. **Budgeted Statement of Cash Flows**

🏠 **Capital Expenditures Budget**

Purpose:

Plans for **long-term investments** (e.g., property, plant, and equipment).

Usually prepared **years in advance** and reviewed **annually**.

Key Features:

- Lists **major approved projects** and the **funds required**.
- Specifies **timing** (quarterly/monthly) of expenditures and cash inflows.

Effects on Financial Statements:

Area	Effect
Balance Sheet	↑ Fixed assets, accounts receivable, inventory, and payables
Income Statement	↑ Revenues from new projects, ↑ Depreciation expense
Cash Budget & Cash Flows	Reflects cash inflows/outflows from projects and financing

Coordination:

Senior management must inform segment managers about planned projects to ensure:

- Proper inclusion in **segment budgets**
- Correct reflection in **financial statements**

📊 **Example Impacts:**

- **New production equipment** → affects fixed assets, depreciation, inventory, and payables.

✅ **Summary**

Element	Description
Budgeting Cycle	Continuous process of planning, executing, and reviewing performance
Master Budget	Consolidated financial plan (Operating + Financial Budgets)
Participative Budgeting	Involves lower management → improves motivation & accuracy
Operating Budget	Includes all components leading to the Budgeted Income Statement
Financial Budget	Includes capital expenditures, cash, and balance sheet planning
Capital Expenditure Budget	Long-term investment plan, impacts all key financial statements